How Canada's banks can help reduce the 'collateral damage' of capitalism

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Body

Royal Bank of Canada, the country's largest bank, participated last month in the massive - $26 billion (U.S.) IPO - of Aramco, the Saudi Arabian oil giant predicted to produce the oil and gas equivalent of 27 billion tonnes of carbon dioxide, more than any other company on earth.

The bank's decision to take part in the IPO, albeit as a junior bookrunner, highlights the tension between doing well and doing good. It made a small profit - an estimated fee of about 2 million riyal (about $700,000 Cdn.) - but in doing so, arguably contradicted its own environmental blueprint.

RBC's CEO, David McKay, wrote to investors recently: "Climate change is one of the most pressing issues of our age - and the financial system needs to be leading efforts to support clean economic growth and the transition to the low-carbon economy." Nice words; and then his bank helps sell shares of the largest oil producer in the world.

With such dissonance, it's no wonder that last Monday, when the World Economic Forum meetings in Davos commenced, Greenpeace accused RBC and 23 additional banking giants of being hypocrites. The veteran environmental group confronted the banks' CEOs with statements of commitment to the environment they made back in 2015 - the year the Paris agreement was signed - and provided evidence that since then, they jointly provided $1.4 trillion (U.S.) to companies active across the fossil fuel life cycle.

According to the report, three of the world's 10 biggest lenders in the oil and gas industry are Canadian banks, with RBC alone accounting for more than $100 billion (U.S.). There is a lot of money to be made in polluting industries, and Canadian banks are well aware of that. They're also not willing to give some of it up. At least not yet.

But recently, we're also hearing different voices in the banking industry. In September, during the UN Climate Action Summit, banks representing a third of the global banking industry officially signed and launched the Principles for Responsible Banking. A total of 131 CEOs of banks signed the historic document, committing to align their businesses with the goals of both the Paris Agreement on Climate Change and the UN's Sustainable Development Goals.

While the CEOs of Canada's Desjardins Group and National Bank are two of the signatories, it is disappointing that none of Canada's Big Five banks (RBC, TD, Scotia, BMO, and CIBC) - who overwhelmingly dominate the Canadian banking industry - saw fit to sign the document.

In fairness, our Big Five banks did step up their game in recent years when it comes to sustainability. They all dedicate sections in their ESG (environmental-social-governance) reports to climate change and show progress. TD for example, has issued since 2014 Green Bonds worth $1.7 billion to finance low-carbon projects. In addition, it has committed $100 billion toward other green initiatives by 2030. RBC also committed $100 billion to sustainable finance by 2025.

These are all important steps, but they pale compared to the magnitude of lending to fossil fuel companies. Our Big Five banks are still captured in a "win-win" paradigm. They've started to make a slow transition to support a low-carbon economy, but aren't willing to make meaningful compromise on their profits. This needs to change.

One person who can help in greening-up our large banks is, interestingly, Canadian. Ex-Bank of Canada governor Mark Carney will be stepping down soon from his role as the Governor of the Bank of England and is set to become the United Nations' Special Envoy on Climate Action and Finance. Carney is known as a climate champion, and was instrumental in establishing the Network for Greening the Financial System, a group of 54 central banks and supervisors who are promoting the transition of the industry toward a sustainable economy. Carney will have a key role in "disciplining" the banks he knows so well.

An additional measure could be for the Bank of Canada to follow Europe and evaluate the impact of introducing a "Green Supporting Factor" and a "Brown Penalty."""> The idea is simple: due to capital reserve requirements, banks will be able to make more money when they lend to firms in green industries.

But the one step that is guaranteed to make a difference is redesigning compensation contracts. If banks' executives will be directly incentivized to reduce the amount of funding to polluting industries, it would actually happen. If Royal-Dutch Shell, the first energy company to link executive pay to carbon emissions implemented it, then with some shareholder activism it could be replicated in banks.

"The brand of capitalism we've seen over the last 30 or 40 years has caused significant collateral damage, including increased inequality and unbridled resource consumption. We need to change course and take a more inclusive approach that ensures the sustainable use of the resources essential to human life." It is not Naomi Klein or Bernie Sanders who are responsible for this statement. It is actually Guy Cormier, the CEO of Desjardins who said it when he signed the Principles for Responsible Banking. Our Big 5 banks should follow suit.

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